

Karen Salmansohn

From: Director - FASB
Sent: Friday, February 14, 2003 12:48 PM
To: Karen Salmansohn
Subject: FW: File Reference No. 1102-001

Letter of Comment No: 282
File Reference: 1102-001
Date Received: 2-14-03

-----Original Message-----

From: Ellis, Jeffrey [mailto:Jeffrey.Ellis@GT.com]
Sent: Friday, February 14, 2003 12:06 PM
To: Director - FASB
Subject: File Reference No. 1102-001

Attached is Grant Thornton LLP's comment letter on the FASB's Invitation to Comment, *Accounting for Stock-Based Compensation: A Comparison of FASB Statement No. 123, 'Accounting for Stock-Based Compensation,' and Its Related Interpretations, and IASB Proposed IFRS, 'Share-based Payment,'* dated November 18, 2002.

If you have any questions, please call Jeff Ellis at (312) 602-8991.

<<GT Comment Letter Statement 123 ITC.doc>>

Accountants and
Management Consultants
The US Member Firm of
Grant Thornton International
National Office
175 West Jackson Blvd.
Chicago, IL 60604-2615
Tel: 312 856-0001
Fax: 312 861-1340

Grant Thornton 

February 12, 2003

Director of Major Projects and Technical Activities
File Reference No. 1102-001
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856

We are pleased to respond to the Financial Accounting Standards Board's (FASB's) Invitation to Comment, *Accounting for Stock-Based Compensation: A Comparison of FASB Statement No. 123, 'Accounting for Stock-Based Compensation,' and Its Related Interpretations, and IASB Proposed IFRS, 'Share-based Payment,'* dated November 18, 2002 (the "ITC").

We believe the intrinsic value model in APB Opinion No. 25, *Accounting for Stock Issued to Employees*, lacks any fundamental principle, which makes it difficult to interpret as new stock-based compensation arrangements are developed, resulting in a need for the FASB and the Emerging Issues Task Force to issue implementation guidance, the volume of which has contributed to the difficulty in applying Opinion 25. While we believe there will be implementation issues associated with applying the fair value method and its adoption will not make all problems with accounting for stock-based compensation arrangements disappear overnight, we believe the model in Statement 123 is preferable to the one offered by Opinion 25. We encourage the FASB to take this opportunity to improve on the fair value method in Statement 123 and, because of our concerns with the Opinion 25 model, we would support requiring adoption by companies for purposes of recognizing stock-based compensation expense. We have the following major comments on the ITC:

- We agree that employees and nonemployees should be treated in the same way and that grant date measurement is generally the most appropriate date to determine the fair value of stock options and awards granted to employees and nonemployees. However, there are circumstances where grant date measurement may not be appropriate.
- The FASB should provide additional guidance to assist preparers in determining expected volatility to address constituent concerns that the expected volatility used in calculating the fair value of a long-term, non-exchange traded option, bears no correlation to the volatility implied in the pricing of publicly-traded options.
- We agree that nonpublic companies should incorporate volatility assumptions in determining the fair value of stock options they grant, but believe more guidance is necessary to assist those companies in determining expected volatility.

- We believe “excess” tax benefits should continue to be recognized in equity but encourage the FASB to improve disclosures so that users of financial statements will better understand the economic impact of option exercises on a company.

Each of these points is discussed further in our responses to the specific questions raised in the ITC.

Issue 1: Statement 123 provides a scope exclusion for ESOPs and certain ESPPs, and the Proposed IFRS does not. Which view do you support and why?

We support a continuation of the scope exclusion in Statement 123 for employee stock ownership plans (ESOPs). ESOPs represent a defined contribution plan, the accounting for which is addressed by FASB Statement No. 87, *Employers' Accounting for Pensions*. AICPA SOP 93-6, *Employers' Accounting for Employee Stock Ownership Plans*, provides guidance on the application of paragraph 64 of Statement 87 to ESOPs. Since ESOPs are subject to ERISA and Internal Revenue Service (IRS) regulations, we believe there is sufficient basis to account for those arrangements in a different manner than other stock-based compensation arrangements. However, we believe the FASB should require ESOPs that are not subject to ERISA and IRS regulations to be accounted for in the same manner as stock-based compensation arrangements subject to Statement 123.

Although we agree with the FASB's rationale for excluding ESPPs from the scope of Statement 123 discussed in paragraph 236 of the Basis for Conclusions, we understand that the desire for convergence between U.S. and international accounting standards and the goal of fewer exceptions in principles-based standards may result in the elimination of the scope exception. We believe a scope exception would be supportable provided the discount offered to employees is not greater than the cost that the issuer would incur to offer shares to the public and the arrangement contains no other features consistent with option arrangements (for example, extended periods of time to exercise or look-back features). Recognizing an expense for the discount, while consistent with the substance of the arrangement (a transaction between an employer and an employee in which the employee receives something of value), would be inconsistent with the accounting for small discounts on stock issued to shareholders and the accounting for fees paid to underwriters in connection with public stock offerings, which are treated as a reduction in the proceeds as opposed to an expense. However, if this exception were the only difference between the proposed IFRS and Statement 123, we would support eliminating it in the interests of convergence.

Issue 2: In measuring the fair value of stock options granted to employees, both Statement 123 and the Proposed IFRS require use of an option-pricing model that takes into account six specific assumptions. The standards provide supplemental guidance for use in selecting those assumptions.

Issue 2(a): Do you believe that an accounting standard should mandate the use of an option-pricing model for measurement purposes? If not, what other approaches do you believe would provide more consistent and reliable estimates of the fair value of employee stock options granted and why?

Yes. We believe the standard should require the use of an option-pricing model.

Issue 2(b): If you agree that an accounting standard should mandate the use of an option-pricing model, do you believe that a particular model should be mandated? If so, which model should be required to be used and why?

We do not believe a particular option-pricing model should be mandated. Rather, the accounting standard should require the use of an option-pricing model that is appropriate given the facts and circumstances associated with the particular award for which the fair value is being determined. We believe allowing the preparer to select the option-pricing model it believes will result in a better measure of the option's fair value is consistent with a move away from rules-based standards. Further, mandating a particular model would have the unintended (and undesirable) consequence of prohibiting a preparer from adopting a future model that may provide a more precise estimate of an option's fair value. Finally, we believe a decision to mandate a particular method for determining the fair value of stock options would be more appropriately made in the Board's fair value project since it addresses financial instrument issues in a broader context.

We believe the standard should:

1. provide a list of option-pricing models available as of the date of issuance and a brief summary of each model, including any unusual option terms that the model has the capability of valuing, and
2. provide guidance on when an option-pricing model should be modified.

Paragraph 22 of the proposed IFRS, *Share-based Payment*, indicates that an adjustment to an option-pricing model would be necessary if the model assumes that an option can be exercised at any time during its life to give effect to the vesting period during which the holder is unable to exercise the option. We believe an adjustment to an option-pricing model would also be necessary if the model assumes the holder of the option can only exercise at the end of the option's life. However, the proposed IFRS indicates no adjustment need be made in the latter circumstance. We disagree with that view since an option that can be exercised at any point after the vesting period has lapsed in some situations has a higher fair value than an option that can only be exercised at the end of its life. A failure to adjust the model in this circumstance would understate the fair value of the option.

Issue 2(c): If you agree that an accounting standard should not mandate the use of a particular option-pricing model, do you believe that additional disclosures should be made to improve the user's ability to compare the reported financial results of different enterprises? If so, what types of additional information should be required to be disclosed?

We believe the FASB should require the following additional disclosures:

1. the option-pricing model selected by the company and, if the company has selected more than one option-pricing model for different plans, why;
2. changes to a different option-pricing model and the reason such a change is considered preferable;
3. how the company defines its employee groups for purposes of estimating expected lives and, if it does not separately define employee groups, why;
4. comparison of expected lives to historical experience of time elapsed after vesting before employees exercise their options, by employee group; and
5. comparison of historical volatility to expected volatility and the reasons for any significant differences.

In addition, we believe disclosures about stock options and awards granted to executive officers (as defined in Regulation C, Rule 405) and board members in relation to total stock options and awards granted to all employees for a period may provide information that is relevant to financial statement users.

Lastly, we recommend modifications to the disclosures required by paragraphs 47d and 47f of Statement 123. We believe the information about significant assumptions used to determine an option's fair value required by paragraph 47d should be disclosed in a tabular format with notes explaining how the significant assumptions were determined. Information about the significant assumptions may currently be provided in paragraph form, making the information somewhat more difficult for users to identify and compare to other comparable companies, while information regarding how the company determined the significant assumptions may not be provided at all. We believe the information about significant modifications required by paragraph 47f should also require disclosure of which option holders benefited from a modification if that arrangement was not extended to all option holders.

Issue 2(d): Statement 123 and the Proposed IFRS require that certain modifications be made to the outcome of an option-pricing model to address certain features of employee stock options. If you believe that other modifications should be made to improve the consistency and reliability of those outcomes, please describe those modifications and why they should be required.

Assuming a company uses an appropriate option-pricing model and inputs, we see no need to modify the results generated by the model. Please also see our response to Issue 2(b).

Issue 2(e): Do you believe that additional guidance for selecting the factors used in option-pricing models is necessary to provide added consistency and comparability of reported results? If so, what types of guidance should be provided and in which areas?

We believe additional guidance on determining expected volatility is necessary. While Statement 123 provides guidance on determining historical volatility, the guidance in paragraph 285 does not provide sufficient help in determining expected volatility. As noted in paragraph 143 of Statement 123, “[e]xpected volatility provides much of the value of options.” Given that and the criticisms leveled about volatility contributing to overstated fair values, we believe the FASB should determine what research is available in the area of determining volatility of long-term stock options and comparing the relationship between historical volatility and volatility implied in the price of exchange-traded options. To the extent existing research in those areas is not sufficiently comprehensive, the FASB should undertake a research project with the goal of providing information to preparers that will help them in determining expected volatility. If the criticisms of volatility assumptions are correct, requiring all companies to recognize stock-based compensation expense under the fair value method will result in information that is neither relevant nor reliable. Just as the minimum value was not acceptable to the Board because that method understates the value of a stock option, a method that overstates the fair value of a stock option as a result of a lack of sufficient implementation guidance should also not be acceptable.

We are not sure the additional guidance would make companies’ results any more comparable given the fundamental differences between companies, but it would certainly improve the reliability of the fair value measurements.

As noted in our response to Issue 2(c), we believe disclosure by a company of how it determines the factors used in the option-pricing model, including how expected volatility compares with historical volatility and expected lives compare with actual lives, would allow users of financial statements to compare reported results.

Issue 3: Do you believe that employee and nonemployee transactions are distinct and, therefore, warrant different measurement dates for determining the fair value of equity instruments granted? If so, why? If not, why not?

No. We believe in many cases there is not a meaningful distinction between employee and nonemployee transactions that warrants different measurement dates. In general, we agree with the recommendation in the proposed IFRS that stock options and awards granted to employees and nonemployees be measured at the grant date.

However, grant date measurement may not be appropriate in all circumstances, such as those seen during the “dot-com” boom where equity arrangements (primarily stock options) were the primary means of compensating employees and the employee received a nominal amount of cash compensation. When a service provider receives only a nominal amount of cash consideration (employee or nonemployee) and either has no other business relationships with the issuer or provides services under an arrangement that is not legally enforceable (nonemployees), we believe changes in the fair value of the stock-based compensation may

influence the service provider's decision to continue providing services, in which case determining the final measure of the cost of that arrangement on the vesting date may be more appropriate. In those circumstances, the grant date may not be a substantive measurement date because the service provider could be influenced by subsequent changes in fair value.

We encourage the Board to develop a model that looks at the substance of the relationship between the issuer and the service provider (be it an employee or a nonemployee) in determining whether a grant date measurement is appropriate. While judgment would necessarily be required to determine when grant date measurement is not appropriate, mandating either grant date measurement or vesting date measurement for all awards would result in treating economically dissimilar transactions in a similar manner, a result that occurs under the current model for measuring the fair value of employee and nonemployee arrangements. For example, EITF Issue No. 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services," requires vesting date measurement for nonemployee transactions, while Statement 123 requires grant date measurement for equity-settled employee transactions, even though in each case the service provider may be in the same economic position. The proposed IFRS provides the opposite result, requiring grant date measurement for all equity-settled arrangements, even if the service provider would only continue providing services if the fair value of the option does not decline. We do not think either result is preferable in all circumstances.

Issue 4: Do you believe that the fair value of equity awards granted to nonemployees that include performance conditions can be measured with sufficient reliability to justify a grant-date measurement method? If so, why? If not, why not?

Yes, when the conditions discussed in our response to Issue 3 are not present, we believe the fair value of the award can be measured with sufficient reliability on the grant date. However, when the arrangement between the issuer and the nonemployee is not legally enforceable and no other business relationships with the issuer exist or consideration other than the fair value of stock options subject to service conditions is *de minimis*, we do not believe the fair value of the awards can be measured with sufficient reliability because the possibility that the nonemployee will choose not to perform if the fair value of the stock options decline is not susceptible to reasonable estimation.

Issue 5: Do you believe the notion of issuance is conceptually of importance in the design of a standard on stock-based compensation? If so, why? If not, why not?

Yes. The issuance date is important because it is the date when the service provider has earned the unconditional right to the consideration. When measuring the fair value of a stock option or award on the grant date is appropriate (see our response to Issue 3), we believe that the failure of the service provider to provide the required services should result in a reversal of expense recognized previously on the forfeited awards. In circumstances where the grant date is not a substantive measurement date, the issuance date is important because that is the date on which the final measurement of fair value would be appropriate.

Issue 6: Do you believe an equity instrument subject to vesting or other performance conditions is issued, as defined by Statement 123, at the grant date? If so, why? If not, why not?

Yes, provided the issuer has an enforceable right to performance. As defined in Statement 123, *issuance of an equity instrument* occurs “when the issuing entity receives ... an enforceable right to ... goods, or services.” We do not believe the fact that an equity instrument is not issued necessarily leads to a conclusion that the *measurement* of the instruments’ fair value should be deferred until it is issued; however, that may be the appropriate conclusion if the facts and circumstances discussed in our response to Issue 3 that would lead to a conclusion that the grant date is not a substantive measurement date are present.

Issue 7: Do you believe that the effect of forfeiture should be incorporated into the estimate of fair value per equity instrument (IASB approach)? If so, why? If not, why not?

We believe that, if a company has the ability to reasonably estimate forfeitures, it should be required to do so under the standard. However, unlike the proposed IFRS, we believe changes in estimated forfeitures should be accounted for as described in paragraph 29 of Statement 123.

We believe requiring companies who have the ability to make reasonable estimates of forfeitures to include an estimate of those forfeitures in determining the expense to be reported in each period will enhance the relevance of reported results. Recognizing a higher level of expense early in the vesting period that, based on history, will be partially reversed in future periods as employees and nonemployees forfeit their awards may impair the ability of financial statement users to determine meaningful compensation trends in the business. Further, requiring companies to make reasonable estimates for purposes of recognizing compensation expense is consistent with the FASB’s approach to accounting for modifications of awards in Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation*. As noted in paragraphs 35 and 36, “[a]tribution of any additional compensation cost may require estimates, and adjustment of those estimates in later periods may be necessary” which we understand to require the use of estimates, when possible, to recognize the additional compensation expense resulting from a modification.

We believe the IASB proposed approach of requiring a company to estimate forfeitures but not allow for “true-up” those estimates will introduce even more measurement uncertainty into the determination of the option’s fair value. We are not convinced that including an estimate of forfeitures that will not subsequently be subject to revision on the basis of better information will result in financial statements that are more relevant. In particular, we are concerned about the impact on smaller companies that may not track employee turnover (either because they don’t have any benefit arrangements that would require them to do so or because the total population is too small to yield a statistically valid estimate); presumably, they will end up recognizing a greater amount of compensation expense.

The process of estimating the effect of forfeitures on the fair value of stock options will also be more complicated than implied in the proposed IFRS. To make the fair value estimate relevant,

companies would need to be able to segregate employees into groups, even if the company assumes that the expected lives of options held by all employees is the same because of the uneven distribution of options within a company. A company that estimated turnover of 20% of its workforce could not just apply that estimate to the total number of awards issued because the turnover is likely to be at the employee level where the number of stock options granted is lower. Doing so would result in understating compensation expense. If the approach suggested by the IASB is implemented, we believe a large number of companies will have difficulty determining employee groups because they have not previously had a need to do so for any other purpose.

Issue 8: Should failure of an award holder to satisfy the conditions that entitle the holder to retain or receive the promised benefits affect the amount of compensation expense that should be recognized related to that award? If so, why? If not, why not?

Yes. We do not agree with the approach to measuring compensation expense in the proposed IFRS. We believe the failure of a service provider to provide all services necessary to be entitled to retain the award should result in reversing compensation recognized previously. We view the accounting for the arrangement in the same manner as the accounting for a cash bonus. If a service provider does not provide the services required to earn (vest in) a cash bonus, the liability is reversed against compensation expense. While we recognize other literature addresses the derecognition of liabilities and that the company has been legally released from its obligation under the bonus arrangement, we believe the same concept should apply to an arrangement that will be settled through the issuance of an equity instrument once the service provider's performance is complete. The proposed IFRS indicates that previously recognized expense should not be reversed when an equity instrument is forfeited, consistent with the IASB's view that the equity instrument has been issued. We do not believe an equity instrument exists (for financial reporting purposes) prior to the time of issuance, even though we believe the fair value of that equity instrument to be issued in the future can be measured with sufficient reliability on the grant date. Reversal of expense recognized on awards that are forfeited because of a failure to fulfill a performance condition is consistent with our view that the issuance date is important.

Issue 9: Do you agree that the result of the IASB's approach to calculate the fair value of equity instruments of nonpublic entities would be closer to fair value than minimum value? If so, why? If not, why not?

Yes. It is unlikely that any company's shares would have zero volatility. However, as noted in our response to Issue 2(e), we believe the FASB should provide additional guidance to help companies determine expected volatility. In doing so, we believe the FASB should provide guidance specifically directed at helping nonpublic companies in determining that estimate.

Issue 10: Which of the two attribution methods described by the standards do you believe is more representationally faithful of the economics of stock-based compensation arrangements and why?

We believe the attribution method prescribed by Statement 123 is more faithful to the economics of stock-based compensation arrangements because the expense is recognized over the period that services are provided and is reversed if the all or a portion of the required services are not provided. However, as indicated in our response to Issue 7, we believe the Statement 123 model should be modified to require those companies that have the ability to reasonably estimate forfeitures to incorporate those estimates in determining the amount of expense to recognize each period.

Issue 11: Statement 123 does not ascribe value to services received in exchange for equity instruments that are later forfeited (that is, recognized compensation expense is reversed upon forfeiture), whereas the Proposed IFRS ascribes value to such services through its units-of-service attribution method (that is, recognized compensation expense is not reversed upon forfeiture). If you support the Proposed IFRS's view, do you believe the units-of-service method ascribes an appropriate value to services received prior to forfeiture? If so, why? If not, why not?

We believe the units-of-service method is a rational and systematic method for determining the amount of compensation expense to be recognized during the period services are being received, but we do not support the way in which that model is applied in the proposed IFRS for the reasons discussed in our response to Issue 8.

Issue 12: Do you believe that the actual outcome of performance awards should affect the total compensation expense incurred by an enterprise? If so, why? If not, why not?

Yes, for the reasons discussed in our response to Issue 8.

Issue 13: Do you believe that this issue [service after vesting] is important in considering an attribution model's validity? If so, why? If not, why not?

No. Consistent with other compensation arrangements, such as deferred compensation contracts, we believe the expense associated with a stock-based compensation award should be attributed to the period over which the service provider is required to perform in order to earn the unconditional right to the award. Although the service provider may continue to provide services after earning the award, the additional services do not give the service provider any additional rights, other than permitting it to delay exercise. If a company believes it is giving away too much value by giving the service provider an extended period after vesting to exercise, it can either shorten the life of the award or increase the time required for the service provider to earn the unconditional right to the award.

Issue 14: Do you believe that the measurement-date criteria in Issue 96-18 accurately reflect the economics of transactions with nonemployees? If not, why not?

Yes, when the circumstances discussed in our response to Issue 3 are present, indicating that the grant date is not a substantive measurement date.

Issue 15: Do you believe that all of the tax benefits derived from stock-based compensation arrangements should be recognized in the income statement? If so, why? If not, why not?

No. The portion of the tax benefit that is contingent upon exercise of a stock option should be recognized as an increase in equity since the transaction giving rise to the benefit is not a compensatory arrangement and the deduction is only received if (when) the holder exercises the option. We believe it follows that, when the benefit is only realized if the option is exercised, it relates to the capital transaction and the allocation of the benefit (between the portion of the benefit related to the amount of expense recognized in the income statement and the excess benefit credited to equity) should reflect that. We see a distinction between a benefit that only arises if a capital transaction occurs and one that arises solely from the granting of an award and think the two should be accounted for in a different manner. The proposed IFRS treats the tax benefits of the two transactions the same, a result we find inappropriate. In addition, we believe recognizing the excess tax benefit in income is inconsistent with the grant date approach to determining the option's fair value.

The following example illustrates a situation where it is difficult to equate the tax benefit with compensation for services provided by an employee. Assume Company grants an option with a four-year vesting period and a 10-year life that is not truncated if Employee leaves after vesting. The option's fair value is \$2 per share on the grant date. Employee leaves after four years when the option is at-the-money. Nine years after the grant date, Company makes a material acquisition and its stock price increases significantly. Employee exercises the option, resulting in Company recognizing compensation expense for tax purposes, even though Employee has not worked for Company in five years. In this illustration, the benefit received by Company in excess of the compensation expense it recognized during the vesting period has nothing to do with services rendered by Employee.

We believe the reporting model is inconsistent in its treatment of tax benefits received on the exercise of stock options (presented as an addition to paid-in capital in the balance sheet, consistent with the view that it is part of an equity transaction, but presented as a cash flow from operating activities in the cash flow statement) and we encourage the Board to address those inconsistencies in its project on the reporting framework. In the short-term, we believe the Board should incorporate the disclosure requirement in EITF Issue No. 00-15, "Classification in the Statement of Cash Flows of the Income Tax Benefit Received by a Company upon Exercise of a Nonqualified Employee Stock Option," of the tax benefit received on option exercises into the disclosures required in the footnote discussing equity compensation arrangements and should require disclosure about how much of the benefit is classified in equity as opposed to a reduction of income tax expense.

Issue 16: As discussed in paragraph 83 of this Invitation to Comment, the Proposed IFRS expands on the disclosure requirements in Statement 123. Do you believe that those expanded disclosures would be more informative to users of financial statements? If so, why? If not, why not? (Which of the disclosure requirements should be eliminated or modified in that case?)

See our responses to Issues 2(c) and 15.

Issue 17: Please describe any additional disclosures that you believe should be required in order to inform a user of financial statements about the economics of stock-based compensation arrangements.

See our responses to Issues 2 (c) and 15.

Secondary Similarities and Differences

Issue A1: Statement 123 distinguishes between a principal stockholder and a stockholder for certain transactions, and the Proposed IFRS does not. Which view do you support and why?

If none of the factors discussed in AICPA Accounting Interpretation 1, "Stock Plans Established by a Principal Stockholder," of Opinion 25 are present, we generally support the view in the proposed IFRS, but are concerned as to whether the benefit from the change will justify the costs companies will incur to obtain information about transactions between a stockholder and an employee. We are not sure whether there are any requirements for a shareholder other than a principal shareholder to report such a transaction. We do not view the percentage of shares owned by the shareholder as being as significant as the reason why, and purpose for which, the shares are granted. As such, we do not believe that the percentage owned should change the accounting for the arrangement. We are not aware of any abuses in this area and we therefore recommend the Board clearly describe the benefits to be obtained if they adopt the view in the proposed IFRS.

Issue A2: Do you believe that a probability-weighted average amount of the range should be used when no amount in the range is better than any other? If so, why? If not, what other amount within the range would you propose when no amount in the range is better than any other? Why?

Although we support a probability-weighted approach as being consistent with the more recent standards issued by the FASB, we do not believe it is clear that such an approach is appropriate when applied to volatility. As indicated in our response to Issue 2(e), we believe additional guidance on determining expected volatility is necessary.

Issue A3: Do you agree that option-pricing techniques have sufficiently evolved since Statement 123 was issued to address reload features and, if so, should Statement 123's requirements be changed? If not, why not?

We are not certain that option-pricing techniques have evolved sufficiently to value reload features, but we believe that the guidance in Statement 123 should be revised to conform to the guidance in paragraph 25 of the proposed IFRS. When the fair value of a reload feature is subject to reasonable estimation, the revised guidance would require measurement on the grant date.

Issue A4: Do you believe there are circumstances in which an entity may not be able to reasonably estimate the fair value of equity instruments at the grant date? If so, please provide examples of such circumstances and describe how those equity instruments should be accounted for until a reasonable estimate is determinable.

Other than the circumstances described in paragraph 21 of Statement 123, we are not aware of other situations where the fair value of an equity instrument may not be reasonably determinable at the grant date. However, there is diversity in views as to whether a company would be able to estimate the fair value of an option whose exercise price will equal the stock price at a specified future date. In the circumstances addressed in paragraph 21 and, possibly, in the preceding sentence, we believe the guidance in paragraph 22 of Statement 123 should be followed until the fair value is reasonably determinable.

Issue A5: Do you believe there is a single grant date or multiple grant dates for the preceding example [in paragraph A17 of the ITC]? Why?

We believe there is a single grant date in the example in paragraph A17 because the employer and employee have a mutual understanding of the terms of the grants that will be made in future years.

Issue A6: Should SARs be measured at fair value rather than intrinsic value? If so, why? If not, why not?

Yes, cash-settled SARs should be measured at fair value. EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," requires the issuer of a cash-settled arrangement to classify the arrangement as a liability, adjust the liability to fair value at the end of each period, and recognize changes in the fair value of the arrangement in income for the period. We do not believe there is any conceptual basis for accounting for cash-settled arrangements held by employees differently from cash-settled arrangements held by nonemployees.

Issue A7: In accounting for equity award modifications, should the fair value of the original award be calculated using (a) the shorter of the remaining expected life of the original award or the expected life of the modified award or (b) the remaining expected life of the original award? Why?

We believe the fair value of the original award at the modification date should be computed using its remaining expected life. Modifications may involve a trade-off where the holder surrenders something of value (a portion of the option's time value) in exchange for something of value (less negative, or more positive, intrinsic value). We believe the incremental increase in the fair value of the option should recognize the fact that the holder may have surrendered something of value. The current accounting model for modifications (paragraph 35 of Statement 123) assumes that only the holder received something of value in the exchange, which may not be consistent with the economics of the transaction.

Issue A8: Do you believe that an accounting standard on stock-based compensation should include provisions for distinguishing between repricing and other modification events? Why?

No. The overriding principle in Statement 123 is to measure awards at their fair value. Applying the principle to modifications requires the issuer to determine if it has provided incremental value to the holder. In that context, it does not matter which of the option's terms have been changed. There is no conceptual difference between repricings and other modifications. However, as noted in our response to Issue 2(c), we believe a company should disclose the terms of any modification that is not extended to all holders of stock options and which holders (or groups of holders) benefited from the modification.

Issue A9: Which method of accounting for settlements of unvested awards do you believe is more representationally faithful and why?

We believe the model reflected in Statement 123 is more representationally faithful. Recognizing previously unrecognized expense when an unvested award is reacquired gives accounting recognition to the fact that the service provider is no longer required to provide services to be entitled to the economic benefits of the award. Continuing to recognize expense after the unvested award has been repurchased could result in an anomalous result if the service provider were to cease providing services. Under the proposed IFRS, the issuer would no longer recognize expense for the fair value of the "services" it will no longer receive. However, the service provider has already realized the value of the unvested award through the settlement. That treatment results in accounting for the settlement of an unvested option in the same manner as a settlement of a vested award.

Issue A10: The Proposed IFRS considers certain factors, including past practice or a stated policy of settling in cash, in evaluating how an entity should account for certain contracts that can be settled in cash or equity, at the entity's option. Do you agree with this view? If so, why? If not, why not?

We agree with the view expressed in the proposed IFRS. We understand that view is also consistent with the view adopted by the FASB in its limited-scope project on distinguishing liabilities from equity on when a contract that provides for settlement in equity should be treated as if it were a cash-settled arrangement. If a company does not have the intent (as evidenced through past practice or its stated policy) of settling an arrangement in equity when it has the choice to do so, we believe the accounting should reflect the substance of the arrangement. Accounting for the arrangement in a manner that conveys the company will elect to settle by delivery of an equity instrument when it is likely it will not deliver an equity instrument does not serve the interests of financial statement users.

Other Matters

We believe the standard on stock-based compensation should discuss the appropriate accounting for stock options (that have a readily measurable fair value) issued to a service provider in exchange for goods or services (that qualify for capitalization and also have a readily measurable fair value) when the fair value of the stock options exceeds the fair value of the goods or services. We assume the incremental value would be recognized as an immediate expense in the absence of some additional value conveyed by the service provider.

We also believe the standard on stock-based compensation should require that each tranche of awards that have graded vesting be viewed as separate awards for purposes of recognizing compensation cost during the vesting period.

* * * * *

We would be pleased to discuss any of our comments with the Board or the FASB staff. Please direct your questions or comments to John Archambault, Managing Partner of Professional Standards, at (312) 602-8701.

Very truly yours,

Grant Thornton LLP